AGL Submission to the Queensland Competition Authority

Review of Electricity Pricing and Tariff Structures Stage 2, Request for Comments Paper

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Table of Contents

Executive Summary

AGL welcomes the opportunity to comment on alternative tariff structure options that would ensure recovery of the costs of electricity supply and encourage more efficient use of electricity, including encouraging demand-side management.

A Network plus Retail (N+R) approach will necessitate the alignment of retail and network tariffs in relation to their fixed and variable components, application criteria and pricing periods. This may require the consolidation of some retail tariffs and the creation of some new retail tariffs to ensure that each retail tariff can be "mapped" to a corresponding network tariff. Further, the QCA is proposing (as per Stage 1 of the review) to develop a new methodology for forecasting the wholesale energy costs and retail costs, which will need to appropriately account for the introduction of the CPRS on 1 July 2011. The QCA will need to ensure that this is done in a way which maintains the existing headroom.

AGL remains concerned that the process for achieving a cost reflective structure under a new pricing methodology is complex, requires extensive consultation with stakeholders, and will require a detailed understanding from the distribution networks as to their proposed tariff structures. AGL is of the view this cannot be achieved in the timeframes proposed by the QCA. Network tariff structures and pricing will not be known until May 2010, making full retail and network tariff alignment very difficult, if not impossible, from 1 July 2010.

AGL remains of the view that the policy objectives articulated in the Ministerial Direction would be most effectively achieved over a longer timeframe, with the 2010-11 year being treated as a 'transitional year', and the establishment of a three year price path commencing on 1 July 2011. AGL previously proposed a transitional approach that would allow a "transitional year", prior to moving to a three year price path and still considers it to be a very constructive approach that should be closely considered. A transitional approach is discussed further in this submission, namely:

- Full pass-through of approved Energex (fixed and variable) network charges from 1 July 2010; and
- Where a retail component is negative for 2009-10, it will be reset to zero as a transition to cost reflective retail tariffs so that only positive differences are escalated; and
- An allowance of an escalation of the retail component of each tariff (calculated as the difference between the notified prices and Energex network from 1 July 2010 based on either CPI or a modified BRCI.

Cost reflectivity of Existing Tariffs

Existing retail tariffs do not generally reflect the underlying fixed costs of supply. With the exception of Tariff 22, and only where the customer's consumption is below 25MWh per annum, retail tariffs do not even fully recover the fixed network charges. To ensure that retail tariffs fully reflect the fixed costs of supply for all customers on a particular tariff, the fixed component of retail tariffs should reflect the full amount of the fixed network charges, retail operating costs, most of which are fixed in nature, and an appropriate retail margin.

Competition across Classes of Customers

As the existing retail tariffs are not cost reflective for smaller customers those customers will be less attractive to retailers. To ensure there is competition for all customers, regardless of their size, it will be important to ensure that the fixed components of retail tariffs reflect the fixed network charges and retail operating costs which are mostly fixed in nature. Consistent with the Ministerial Direction, it will also be important to ensure that for each tariff the level of headroom is sufficient to foster effective competition, the level of headroom remains relatively stable, and retailers do not incur a loss in providing retail services to regulated customers.

Customer impacts from tariff reform

The process of tariff reform will require an assessment of the impact on customers of any proposed changes to tariffs. Adverse financial impacts on customers should be addressed through direct and transparent rebates from Government where it is considered warranted. Achievement of social policy objectives through 'smearing' of costs across customer classes, or through suppression of prices will continue to stifle network price signals to customers regarding their consumption of electricity.

Large customers

AGL supports the QCA's recommendation that price regulation for large customers consuming more than 100MWh per annum should be removed from 1 July 2010 so that the market can develop the necessary products that properly reflect each customer's cost of supply, based on their actual load shape. Large customers of Tier 1 retailer are included in the Net System Load Profile (NSLP) whereas customers of Tier 2 retailers are required to be on interval meters. This creates complexity in regulating a group of customers that typically have distinctly different load profiles.

Need for new tariffs

Implementation of an N+R approach will require each retail tariff to have only one corresponding network tariff and the criteria for application to be aligned. Energex has a separate network tariff depending on whether the customer consumes more (medium) or less (small) than 25MWh per annum, whereas there is currently no such distinction in the retail tariffs. Therefore, new retail tariffs will need to be created to ensure the available retail tariffs can be matched to a network tariff.

Time of Use Tariffs

AGL understands there are a significant number of customers in the Energex region with Time of Use (TOU) metering that is capable of measuring consumption at half hourly intervals. AGL understands the existing TOU meters are read as accumulation (Type 6) meters. AGL is of the view that, with appropriate stakeholder consultation, the existing suite of tariffs could be complemented over time by the introduction of TOU network and retail tariffs for residential customers.

Inclining Block tariffs

AGL acknowledges that in the absence of a TOU tariff, inclining block tariffs (IBT) may provide a (muted) price signal to customers that may encourage them to reduce peak demand. Inclining block tariffs were introduced in South Australia, Victoria and NSW by the distribution network providers in an attempt to provide a pricing signal to customers who do not have access to TOU metering. AGL is of the view that an inclining block tariff will have some merit as a transitional measure until TOU tariffs can be introduced. It will be important to ensure that blocks are set at levels that are designed to reduce inefficient consumption but do not penalise those customers whose consumption is relatively inelastic.

In the event that the distribution networks seek to introduce an IBT for residential customers it will be important to ensure that the main residential retail tariff is aligned so as to allow the direct pass through of all network charges.

Tariff Consolidation

From 1 July 2010 customers on Tariff 21 should be transferred to Tariff 20. AGL is of the view that a declining block tariff is inappropriate and as there a relatively small number of customers on that tariff it should be closed from 1 July 2010.

Whilst AGL is of the view that customers on obsolete and less common tariffs should be able to be transitioned to other more common tariffs, AGL is unable to assess the likely revenue and price impacts of their transition as the pricing periods for those tariffs differ from Tariff 22. Such an assessment would require information on the consumption of customers on these tariffs (37, 62 63 64 65, 66,) in the Tariff 22 pricing periods. AGL notes however, that whilst there are only relatively small numbers of customers on these tariffs, the pattern of consumption between peak and off-peak periods can significantly affect customers' bills and retailer revenue. Average consumption on tariff 37 is higher than on the "farm" tariffs so timing of consumption is more likely to affect existing Tariff 37 customers.

Transitional Approach

As stated above, AGL is of the view that the policy objectives articulated in the Direction will be most effectively achieved over a longer timeframe, with the 2010-11 year being treated as a 'transitional year', with a view to establishing a 3 year price path commencing on 1 July 2011. The QCA would then have the time necessary to properly consider:

- The appropriate methodology for determining the WEC in circumstances where the details of the CPRS will be known and can be more comprehensively dealt with. A three year price path commencing in 2011 is less likely to require comprehensive overhaul;
- A comprehensive restructure of the tariffs, considered in light of the network tariff structures (which will not be known until 30 May 2010). The AER will make a determination on the next 5 year price path for both Energex and Ergon, with both determinations becoming effective on 1 July 2010. This is likely to entail a 'P-0' adjustment, and significant restructure of the network tariffs AGL suggests that any comprehensive restructure of retail tariffs is going to be achieved more efficiently and smoothly if the network tariff structures are known and relatively stable. While the network tariffs will not be completely stable during the 5 year price path, it may be assumed that the 'step change' will occur at the commencement of the period. It therefore seems sensible to conduct the overhaul of retail tariffs once this network tariff structure is known; and
- The most appropriate means of managing the customer impacts resulting from the move to cost reflectivity and demand management price signals. AGL suggests this part of the process will need to be the subject of intensive consultation between the QCA, industry, consumer groups and the government.

It is also necessary to consider the impact time constraints have had in the past on the development of the BRCI methodology and its subsequent applications. Similar difficulties should be minimised if sufficient time is allowed for thorough consultation with all stakeholders at all stages of development and implementation of the alternative methodology.

<u>Approach for Transitional Year</u>

AGL is suggesting an approach whereby:

- Network tariffs are 'excised' from the existing retail tariffs, thereby identifying an 'N' component and a 'R' component, which are both comprised of fixed and variable components;
- Where there are two (or more) possible 'N' components the <25MWh network tariff would be used;
- Where the 'N' fixed component exceeds the 'R' fixed component, the R should be adjusted up to $0 ;
- The R component is then indexed, either in accordance with CPI or the BRCI adjusted to exclude the networks
    - CPI Approach: the R component could be adjusted by the relevant quarter on quarter CPI, or the average CPI for the year.
    - BRCI Approach: as detailed in AGL's response to the Issues Paper, the BRCI could be amended to so as to remove the reference to network tariffs, and the 'remainder' of the BRCI be used to calculate the rate of change applicable to the R component. The legislative framework would require relatively simple amendment to exclude the networks from the BRCI calculation (see below).

This would permit the QCA to use its current methodology to determine the rate of change in the WEC and the operating costs. While this is not the optimal result for retailers operating in the Energex patch, it provides a means of ensuring a robust, consultative process capable of avoiding further controversy and uncertainty in the available time.

In this way, the QCA can commence a process of tariff adjustment and maintain the uniform tariff policy, while avoiding the need to make assumptions as to how networks will adjust their tariffs (discussed elsewhere in this submission) and avoiding the need to develop a new wholesale methodology in an insufficient time period. AGL is aware that there are issues with this simplified approach especially due to the mismatch of network and retail tariffs. As this would only be a transitional matter, AGL believes that these issues can be managed. This approach to transitional pricing should be viewed in the context of the likely significant price increases with the introduction of CPRS.

Legislative Change

AGL recognises that any variation from the current BRCI methodology would require legislative change. AGL has previously suggested[1] a legislative approach which will:

- Provide in legislation the key principles which must underpin the regulation of the retail price of electricity for small non-market customers;
- Permit the making of regulations which will further specify the process and regulatory principles – thereby providing greater direction through regulation while allowing greater innovation and flexibility in the future;
- Permit flexibility around the commencement of the 3 year price path so as to cater for the option of a 'transitional year' approach, whereby elements of the BRCI would be used for a 'transitional year';
- Establish a robust review process in line with that provided in other jurisdictions.

Large Customers

AGL notes and supports the QCA recommendation for regulated pricing to be removed for large customers consuming more than 100MWh per annum from 1 July 2010. As noted in previous submissions, retailers are subject to significant risks associated with permitting these customers to remain on the regulated tariff, including the risk of acquiring cover for these large un-contracted loads that could churn away without notice.

The regulation of prices for this category of customers is complex and unlikely to ever yield a cost reflective outcome as the load profiles and size of these customers vary significantly. Currently in Queensland large customers of Tier 2 retailers are required to be interval metered whereas large customers of the Tier 1 retailer may remain on "dumb" meters. Accordingly Tier 1 customers' consumption data is currently included in the Energex NSLP, which has the effect of distorting the Energex NSLP. If the NSLP is used to set prices for large customers it will result in a skewed outcome between Tier 1 and Tier2 retailers; the Tier 1 retailer will settle its energy purchase costs on the NSLP (match) whereas Tier 2 retailers will settle based on the costs associated with the actual load profile for their customers (mismatch). Whilst some large customers may have large flat loads, others (e.g. shopping centres and air conditioned apartment and office buildings) will have a load profile that is significantly peakier than the NSLP thereby leading to the under-recovery of energy purchase costs for customers of Tier 2 retailers.

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[1] In AGL's Further Submission to the QCA dated 4 August 2009

Other ongoing difficulties with existing Notified Prices for large customers are:

- Existing retail tariffs for large customers are not matched by a corresponding network tariff, the minimum chargeable demand thresholds are not aligned with those of the network, and Tier 2 retailers are currently prohibited from passing through costs such as metering charges and other site specific charges.
- Energex has signalled its intention to introduce a kVA (demand) tariff from 1 July 2010 for customers consuming 1 July 2010. Customers with a 'good' power factor will receive a discount, while customers with a poor power factor will pay a premium. The effect of a change to kVA tariffs will therefore be a redistribution of each customer's contribution to the total revenue recovered from each customer class.

If regulated pricing is removed for this group of customers and they are required to move onto market contracts, each customer will be offered a market price that reflects all the costs associated with their load profile. Whether a customer's prices increases or decreases will depend on their particular load profile and how that compares to the NSLP.

In the event that regulated prices are not removed from 1 July 2010, an adjustment would be required to the NSLP for the impact of large industrial customers. Additional new retail tariffs will also need to be created to match the available network tariffs. AGL would welcome the opportunity to discuss these issues further with the QCA.

Alternative tariff structures to support cost reflectivity

1. The makeup of individual tariffs

1.1 Do the fixed charges currently specified in the existing tariffs reflect the fixed costs incurred by retailers (other than network costs) when supplying retail electricity services to customers on those tariffs, including customers with little or nil consumption?

The fixed component of retail tariffs generally do not fully recover the fixed costs incurred by retailers. The fixed charges on the main residential tariff, Tariff 11, and large business (demand) Tariffs 41 and 43 are not sufficient to even fully recover the fixed component of the underlying network charges (see Table 1 below).

With the exception of Tariff 22, and only for customers consuming less than 25MWh per annum, no retail tariffs recover the fixed retail operating costs.

Table 1: Comparison of Fixed Charges

Residential Supply	Retail Tariff 11	Network Tariff 8400(<25MWh)	Network Tariff 8600 (>25MWh)
Fixed charges p.a.	$79	$93	$407
Large General Supply (Demand)	Retail Tariff 41 (75kW)	Network Tariff 8300 (20kW)	Network Tariff 8200 (120kW)
Fixed Charges p.a.	$483	$681	$5,057
Large General Supply (Demand) TOU	Retail Tariff 43 (400kW)	Network Tariff 8100 (400kW)	
Fixed Charges p.a.	$483	$13,693	

1.2 *If not, which of the existing tariffs have fixed charges that are the closest to cost reflectivity and which fixed charges are the furthest from cost reflectivity?*

Ideally, fixed charges in the retail tariffs should reflect the fixed network charges plus retail operating costs and a retail margin. The majority of the existing retail tariffs do not reflect this with most retail fixed charges falling well short.

Tariff 22 is the only notified tariff with a fixed charge that has a positive margin after recovery of the network fixed charge and retail operating costs (based on benchmarks allowed for in 2009-10 BRCI.

Table 2: Comparison of Fixed Charges – Tariff 22

General Supply TOU	Retail Tariff 22	Network Tariff 8700 (<25MWh)	Network Tariff 8700 (>25MWh)
Fixed Charges p.a.	**$315.84**	$93.38	$407.29

Tariff 11 has a fixed charge which does not even fully recover the fixed network charge.

In addition, there are issues with the structure of a number of tariffs such as Tariffs 21, 31 and 33 which have minimum payments whilst the underlying network tariffs have fixed charges.

1.3 *Should the retail (non-network) prices include a fixed cost component as well as a variable cost component?*

To accurately reflect the costs of supply, the retail prices should include both a fixed cost component to reflect retail operating costs, which are mostly fixed in nature, and a variable component which reflects those costs and risks in particular, wholesale energy costs, which vary with usage. Retail margin may be recovered in the variable rate or through both fixed and variable rates.

1.4 *What alternatives, if any, are available for aligning network tariffs with retail tariffs?*

New retail tariffs would need to be created if each network tariff is to have a corresponding retail tariff. The application criteria and peak/off peak periods for each network and retail tariff would also need to be aligned to ensure network pricing signals are not stifled. AGL again notes that this will be extremely difficult to achieve in the timeframes currently proposed given the networks will not publish their restructured tariffs until end of May 2010. Other alternatives for alignment of network and retail tariffs are not apparent.

<u>Large Customers</u>

The current schedule of Notified Prices does not provide an appropriate selection of retail tariffs that reflect the risks and costs associated with supplying large customers. It can be seen from Table 3 below that, subject to a customer's consumption and demand level, Tariffs 41 and 43 do not reflect the underlying network charges.

The minimum chargeable demand thresholds of the retail and network tariffs are not aligned. If large customer tariffs are not removed from the schedule of Notified Prices from 1 July 2010 an additional tariff would need to be created so each retail demand tariff has a corresponding network tariff. Each tariff should also be amended to allow pass through of metering and other site specific charges.

Table 3: Comparison of Large Customer Tariffs

Large General Supply (Demand)	Retail Tariff 41 (75kW)	Network Tariff 8300 (20kW)	Network Tariff 8200 (120kW)
Fixed Charges p.a.	**483.48**	681.10	5,057
Min demand charge $/kW/month	**28.28**	13.53128	8.77622
Min demand charge p. m.	**2,121**	271	1,053
Usage c/kWh	**5.95**	1.292	1.284
Large General Supply (Demand) TOU	**Retail Tariff 43 (400kW)**	**Network Tariff 8100 (400kW)**	
Fixed Charges p.a.	**483.48**	13,693	
Min demand charge $/kW/month	**12.24**	7.54127	
Min demand charge p. m.	**4,896**	3,017	
Usage c/kWh – peak	**12.1**	1.329	
Usage c/kWh – off peak	**4.84**	1.329	

2. The suite of tariffs available to customers

2.1 Which of the existing tariffs are closest to achieving cost reflectivity and why?

The level of cost reflectivity of the existing tariffs can only be properly assessed once the appropriate costs incurred by retailers have been established (ie energy purchase cost, retail operating costs and appropriate margin/headroom). None of the tariffs are close to cost reflectivity at an individual customer level. AGL is happy to discuss individual tariffs with the QCA on a confidential basis.

2.2 Which of the existing tariffs are furthest from achieving cost reflectivity and why?

The level of cost reflectivity of the existing tariffs can only be properly assessed once the appropriate costs incurred by retailers have been established. AGL is happy to discuss individual tariffs with the QCA on a confidential basis.

2.3 Is the existing schedule of tariffs sufficient to achieve cost reflectivity or should further tariffs be added (or deleted)?

Existing Tariffs

There is an opportunity to consolidate or simplify a number of retail tariffs on the basis of similar pattern of usage and the small number of customers currently on the relevant tariff(s).

- Whilst AGL is unable to assess likely revenue and price impacts regarding the transition of customers on Tariffs 62, 63, 64, 65 and 66 to Tariff 22 (as the pricing periods for those tariffs differ) there are only a small number of customers on these tariffs with very small levels of consumption. AGL has no customers on Tariffs 53 or 67.

- Declining block tariffs (eg Tariff 21) are inappropriate in peak periods as they send perverse price signals to customers and stifle the ability of networks to send efficient price signals. AGL has only a small number of customers on Tariff 21 and considers that they should be transferred to Tariff 20.
- The domestic network tariff (Tariff 8400) applies to residential customers who consume up to 25MWh a year whereas the main residential retail tariff (Tariff 11) applies up to 100MWh a year. Consideration should be given to aligning the tariffs so that Tariff 11 will also apply only to residential customers consuming up to 25MWh and Tariffs 20 or 22 will apply to those residential customers who consume more than 25MWh a year.

New Tariffs

AGL understands there are a large number of meters now installed in the Energex region that are capable of measuring half hourly data but are currently read as Type 6 (accumulation) meters. A TOU tariff for residential customers should be developed for future implementation so that customers have an incentive to shift demand from the (expensive) peak to the off peak period. This can only occur if a TOU tariff is also developed by the network. Sufficient time is required to ensure data collection and pricing is properly established and customers are provided with information to enable them to understand the benefits (and risks) associated with such a tariff. In this regard, AGL notes that, in NSW, Energy Australia (network and retail) has closed its flat tariff to new residential customers and only offers TOU tariffs to new customers and those existing customers who move to different premises with a meter capable of measuring the relevant time periods.

If customers consuming more than 100MWh a year continue to have access to regulated prices, it will be necessary to create a third demand based retail tariff to align with the range of network tariffs. New kVA (demand) tariffs will also need to be created from 1 July 2010 to align with the new network tariffs to be introduced by Energex. Notified prices should be amended to allow all metering and other site specific charges to be passed through in full.

2.4 What types of tariffs would ideally be included in the tariff schedule?

For small customers, AGL supports the following types of tariffs (depending on meter installation):

- Anytime (flat) rate;
- TOU (with peak & off-peak rates); and
- Controlled Load.

These tariffs may include an inclining block or seasonal structure.

Anytime and TOU types of tariffs are currently available to small business customers provided an appropriate meter is installed. Currently, only the "anytime" rate is available to residential customers along with controlled load (Tariffs 31 and 33). Where appropriate meters are installed, TOU tariffs should be introduced to residential customers.

2.5 Regarding the conditions that restrict the uptake of certain regulated tariffs, are there any conditions that should be changed or relaxed to allow or encourage more customers to take advantage of time-of-use tariffs, controlled load tariffs or other types of tariff that may be considered more cost reflective?

The application criteria for retail tariffs should be aligned with those of the related network tariff. There is no disadvantage in expanding controlled load Tariffs 31 and 33 to allow a greater variety of appliances to be connected to these tariffs, provided customers are informed of the limitations imposed by the tariff.

As noted above, Tariff 11 should be restricted to residential customers consuming up to 25MWh a year to align it with the domestic network tariff (8400).

3 Promoting competition across classes of customers

3.1 Is there a greater level of retail competition evident for certain classes of customers? If so, what makes these types of customers more attractive for competition?

Current notified prices are weighted towards higher variable charges with very small (or no) fixed charges. As most retail tariffs currently do not reflect the fixed costs of supply, customers who consume very small volumes will not generally be paying the full cost of their electricity supply and therefore retailers (and larger customers) will be subsidising those customers. Therefore smaller customers will be less attractive to other retailers as they will deliver smaller or negative margins. Those customers consuming higher volumes and higher margins will be attractive and more likely to receive market offers.

In order to ensure all customers attract competitive offers it will be necessary to ensure that the fixed component of retail tariffs reflect underlying costs for all customers ,regardless of size, and an appropriate retail margin that maintains headroom for retailers.

3.2 Are certain classes of customers, on average, currently on tariffs closer to cost reflectivity than others? Why?

Without first establishing the actual costs of supply, it is difficult to comment on which tariffs are likely to be cost reflective. However, Tariff 22 for customers consuming less than 25MWh a year does recover the fixed network charges.

3.3 How should the Authority best determine the prices necessary to promote competition for each customer class?

The fixed component of the retail price should fully reflect the fixed costs faced by retailers (i.e. fixed network and retail operating costs) and a reasonable retail margin. The variable component of the retail tariffs should only reflect those costs that move with consumption (e.g. energy purchase costs). Consistent with the Ministerial Direction, prices should also maintain sufficient headroom to foster effective competition and headroom should remain relatively stable. The structure of tariffs should not result in retailers providing services to any regulated customers at a loss.

<u>Large Customers</u>

Notified prices for large customers consuming more than 100MWh per annum should be removed and the competitive market allowed to determine its own solution. Currently, retailers can only choose from the Notified Prices and, unlike in other States, are prohibited from passing through site specific and metering charges imposed by the network. In all other states large customers negotiate their own market contracts.

3.4 If prices are made cost reflective, are there any reasons why notified prices should not be retained for small and/or large business and commercial customers?

Small Customers

Provided notified prices are set at fully cost reflective levels with an appropriate retail margin it can represent a safety net for a customer that protects them against the volatility of the wholesale market. However, it must be recognised that in price regulation processes, a regulator is attempting to forecast the costs incurred by a retailer operating in a volatile market characterised by significant risk. This creates a clear 'asymmetric risk' in a competitive market, as discussed by AGL in previous submissions.

Further, as clearly articulated by the AEMC in its recent report [2] these risks will increase dramatically with the introduction of the CPRS and an expanded RET. As noted by the AEMC:

> *For the reasons discussed above, volatility in carbon, and therefore electricity, costs is likely to be significant. It will be difficult for pricing regulators to accurately predict the future impact of carbon costs on electricity costs when setting electricity prices. The likelihood of significant variances between carbon-inclusive energy costs allowed by a pricing regulator and actual costs is high in this environment.*
>
> *One view of CPRS costs is that they are like any other cost or market volatility that a retailer is required to manage. Therefore, these costs should be dealt with through regulatory frameworks without change to existing mechanisms. We do not agree with this view. The magnitude of the likely cost change and the potentially limited capacity for hedging these costs will, in our view, make the issue substantially different to other forms of cost volatility that pricing regulators address in setting tariffs.*

AGL maintains that the preferred regulatory approach should be that adopted in Victoria, where prices are de-regulated (with a reserve power to regulate pricing).

Large Customers

As previously noted, prices should not be regulated for large customers consuming more than 100MWh a year.

4 The removal and consolidation of tariffs

4.1 Should the three existing tariffs that are labelled obsolete in the tariff schedule be removed, and if so, what are the implications of doing so?

Tariff 63 can be consolidated into Tariff 62 (initially) or Tariff 22 (eventually) as they have the same pricing periods. Customers with low usage will face significant price increases.

[2] Review of Energy Market Frameworks in light of Climate Change Policies 2nd Interim Report 30 June 2009, pages 49-59

On the other hand, Tariffs 37 and 64 have peak and off-pricing periods which do not correspond with those of the corresponding network tariffs and hence network and wholesale energy costs attributable to these tariffs are unlikely to be cost reflective. If these tariffs are to be consolidated into Tariff 22, the clocks on these meters may need to be re-set. AGL understands that some clock changes may be performed remotely by the network operator but there will be some meters which require a site visit to physically re-set the clock. In addition, to understand the impact on customers and retailers, further analysis will be required to assess the consumption in the new peak and off peak pricing periods.

4.2 What criteria should be used to consider which tariffs to consolidate?

AGL considers that the following factors should be taken into account when consolidating tariffs:

- Type of meter installed at a premise will limit the types of tariffs which may be consolidated. Meters with dual registers for peak and off-peak usage allow both TOU tariffs and anytime tariffs, while meters with a single register only allow anytime tariffs.
- Tariffs with similar characteristics such as tariff structures, underlying network costs and pricing periods might be consolidated. Minimum payments should be replaced by fixed charges.
- Tariffs with relatively few customers might be consolidated to reduce administration cost and complexity.
- Costs of consolidating tariffs should also be minimised, for instance, a site visit may be required to re-set the clocks.
- Financial impact on customers and retailers is a relevant consideration.

4.3 Which of the existing tariffs should be consolidated?

In general, non-residential usage should be consolidated into either Tariff 20 for anytime (flat) rates or Tariff 22 for TOU tariffs. Aside from the obsolete tariffs:

- Tariff 21 has a minimum charge per month instead of a fixed charge, and a declining tariff block structure which has been set up with much higher priced first blocks to compensate for the absence of a fixed charge. Given that Tariff 21 is an anytime tariff, it could be consolidated into Tariff 20.

- Tariff 62 is a TOU tariff with pricing periods similar to Tariff 22 but with a declining block structure. A consolidation into Tariff 22 is a reasonable proposal provided any revenue losses are balanced by the adjustment to Tariff 22 rates.

5 Alternative tariff structures to encourage efficient use of electricity

5.1 What should be the relevant considerations when choosing alternative tariff structures that promote demand management and energy efficiency?

Tariff structures that closely reflect the underlying costs of supply will ensure there is equity between customer classes (i.e. avoidance of cross subsidies between customers) and promote the efficient use of resources. Other important considerations are the ease with which alternative tariff structures can be implemented and easily understood by customers.

5.2 *What impacts will peak and off-peak pricing have on various customer classes? What classes of customers are likely to be affected most?*

Customers who are generally able to shift their consumption from the peak period to the off peak period, and who are sensitive to price, will benefit most from TOU pricing. Those (typically small) customers with relatively inelastic consumption may be adversely impacted by TOU pricing if they are unable to move their consumption to an off-peak period.

5.3 *To what extent could network tariff reforms better address demand management objectives rather than retail tariff reform?*

Network reform cannot of itself deliver demand management objectives. Network tariff reform will only be effective to the extent that price signals from the network are reflected in retail tariffs. Network tariff reform is unlikely to have any impact unless matched by retail tariff reform.

5.4 *How should the Authority ensure that the structure of tariffs does not impede the existing initiatives of distributors in managing peak demand?*

To ensure that network price signals are not stifled, the structure of retail tariffs, pricing periods and application criteria would need to be aligned with network tariffs.

6 Inclining block tariffs

6.1 *Would the introduction of an inclining block tariff structure deliver significant benefits (in terms of more efficient use of electricity and reduced peak demand) by itself?*

As noted by the QCA in its Request for Comments Paper, inclining block tariffs (IBT) have been promoted, and adopted, as an alternative solution to the inability of flat tariff structures to provide a signal about the value of electricity to users. IBTs have been introduced by the distribution network providers in South Australia, Victoria and NSW.

AGL acknowledges that in the absence of a TOU tariff, IBT may provide a somewhat muted signal to customers that will encourage them to reduce overall consumption, with a possible flow on impact to peak demand.

An appropriately structured IBT will provide a more efficient price signal than the existing flat tariffs. In the event that the distribution networks seek to introduce an IBT for residential customers it will be important to ensure that the main residential retail tariff is aligned so as to allow the direct pass through of all network charges. AGL considers that any new tariffs must be developed with full consultation with all stakeholders to ensure that the outcome is both cost reflective and sustainable.

Appropriate metering permitting, AGL would generally favour the introduction of a TOU tariff over an IBT, as a more effective means of encouraging consumers to reduce peak demand. Until such time as an appropriate TOU tariff is available, an IBT may provide a better price signal to customers than the current flat tariffs.

6.2 *Would an inclining block tariff structure be more suited to some tariffs than others? Which ones?*

An IBT would be most appropriate for tariffs which currently do not provide any price signal, i.e. anytime (flat) tariffs due to meters with a single register. The IBT structure would be particularly suitable for Tariffs 11 and 20.

The IBT structure need not be limited to anytime tariffs. It could be used to accentuate the pricing signal of TOU tariffs by building this tariff structure in the peak pricing component possibly in combination with a declining block structure in the off-peak pricing period.

It is important that the underlying changes in tariff structure are firstly created in network tariffs.

6.3 *What thresholds would be appropriate for each of these tariffs in order to provide appropriate pricing signals?*

The second block of an IBT should be set at a level that is designed to reduce inefficient consumption but maintains affordability of electricity for an average level of electricity. An IBT should set the second block at the median consumption level for residential customers, i.e. about 4 MWh a year (54^{th} percentile).

A further threshold should be set at 12MWh a year (95^{th} percentile).

Tariff	Block	Threshold
Tariff 11	**1^{st}**	0 – 4MWh p.a.
	2^{nd}	4 – 12MWh p.a.
	3^{rd}	12 – 100MWh p.a.
Tariff 20	**1^{st}**	0 – 25MWh p.a.
	2^{nd}	25 - 100MWh p.a.

7 Peak demand and time-of-use pricing

7.1 *How widely available are time-of-use meters and to what types of customers?*

AGL does not have sufficient information to comment but notes that less than 2% of its electricity customers in Queensland are currently on a time-of-use tariff. AGL understands that currently nearly 20% of meters can measure peak and off-peak usage although most of them are billed on a flat tariff structure. Currently, there is no TOU tariff for residential customers.

7.2 *Would the availability of peak pricing and time-of-use tariff structures deliver significant benefits (in terms of more efficient use of electricity and reduced peak demand) given the existing availability of the required metering?*

AGL understands that increasing number of TOU meters are being rolled out so that the opportunity to provide time-of-use pricing signal continues to grow.

7.3 Should time-of-use metering be encouraged and, if so, how?

TOU pricing is a more effective signal than inclining block structures to encourage customers (who are price sensitive) to shift the timing of their consumption. A residential TOU tariff can only be introduced if there is a corresponding network tariff. Consideration should be given to closing the flat residential and business tariffs to new customers who have TOU meters and to existing customers who move to premises that have a TOU meter.

In determining a TOU tariff an assessment of the WEC component will be required to provide a properly structured tariff that would gives the appropriate price signals and appropriately values the variation in costs of managing risks in the wholesale energy market. This assessment is a complex one and needs to be undertaken through a robust and transparent process with full consultation with industry stakeholders.

8 Interruptible tariffs

8.1 How effective are interruptible tariffs and/or individual control devices in managing customer demand during peak demand periods?

AGL is unable to answer this question. However, it should be noted that interruptible tariffs are a network driven initiative and the timing of when supply is interrupted is a function of network capacity rather than pool electricity prices. Retailers have no opportunity to influence the timing of when supply is interrupted or to receive sufficient notice of the times of the likely interruptions. Retailers settle their energy purchase cost for small customers based on the NSLP and therefore interruption of supply has no impact in the short term on a retailer's energy purchase costs.

8.2 To what extent have customers in each distribution area that have the capacity to access an interruptible tariff taken up the option?

AGL is unable to answer this question.

8.3 What types of consumption would be suitable for interruptible tariffs and/or individual control devices?

AGL is unable to answer this question.

8.4 What are the metering requirements for hard wired appliances and those using individual control devices?

AGL is unable to answer this question.

8.5 Would a wider availability of interruptible tariffs and/or individual control devices enabling remote load control be an effective means of managing periods of peak customer demand? Which would it be more cost effective?

AGL believes that further trials and analysis will be required to assess the costs and benefits of interruptible tariffs and control devices. Interruptible tariffs generally benefit the network in times of peak demand and customers where there is a reduction in network charges by utilising these tariffs. There is little benefit in relation to energy purchase costs as retailers are still required to settle the market based on the NSLP.

9 Other demand management initiatives

9.1 What other demand management initiatives are being undertaken by industry?

AGL is unable to answer this question.

9.2 Are such schemes capable of being integrated with any of the identified alternative tariff structures?

AGL is unable to answer this question.

9.3 Are alternatives to the existing tariff structures necessary for such other demand management initiatives to be successful?

AGL is unable to answer this question.

10 Transitional arrangements and future options

As previously noted in this submission, AGL considers a "transitional" approach should be adopted for 2010-11 with a full three year price path to commence from 1 July 2011. AGL remains very concerned regarding the time available to conduct a full review of prices under a new methodology.

10.1 How should the Authority ensure that the structure of the notified tariffs will allow or complement the future use of smarter meters and similar technology?

Consideration should be given to the development of a TOU tariff (in consultation with the networks) for implementation at a future date. It will be important to ensure that sufficient half hourly consumption data is available to construct a load profile for customers with TOU meters. Consideration should also be given to an appropriate time at which the existing (flat) residential tariff should be closed to new customers.

10.2 What transitional arrangements should the Authority consider to allow customers affected by any change the opportunity to respond to any changes that result from tariff restructure and the introduction of cost reflective tariffs?

It will be important that all customers are provided with sufficient information and notice regarding any potential changes to tariff structures and types to allow them to adjust their consumption behaviour. For this reason AGL is of the view that no substantive changes be made to tariff structures for 2010-11 (e.g. inclining block or TOU tariffs) to ensure that sufficient time is available for full stakeholder consultation and a robust process for the development of new tariff structures and retail prices. However, in the event that the distribution networks create new tariffs from 1 July 2010 new retail tariffs may be required to ensure network costs can be passed through in full.

AGL is of the view that vulnerable customers experiencing price increases through the introduction of cost reflective tariffs should be assisted through direct subsidies from Government. Any deferral of cost reflective pricing will simply delay the ability of the networks to pass price signals to consumers and stifle any existing demand side management initiatives.